NOTES

WASHINGTON NOTES

THE COMPLETION OF THE "LIBERTY LOAN"

The completion, on August 30, of the period within which subscriptions to the government loan of $2,000,000,000, offered to the public in May and June, were to be paid, now for the first time permits some more or less accurate estimate of the power of the United States to provide for the maintenance of the war with Germany. Probably the first consideration in this connection that presents itself is the remarkable and more than expected success attained in connection with the loan itself. The fact that, in round numbers, $3,000,000,000 instead of $2,000,000,000 was offered is an interesting, but by no means the most important, feature of the transaction. The most striking aspect of the situation is found in the fact that the diversion of the $2,000,000,000 actually accepted in subscriptions to government uses did not, in any apparent degree whatever, disturb the financial markets of the country. This, in a large measure, is due to the working of the federal reserve system, under which it was possible, not only to retain all of the subscription funds in the banks in which they originated, but also to transfer the subscriptions for bonds from the private holders of the funds to the government, and from the latter to the sellers of goods or to the foreign governments to which they were advanced, without altering the distribution of the nation's cash. The operation of the Gold Settlement Fund at Washington entirely obviated any necessity for shipments of currency or specie from one part of the country to another, and thus the whole transaction was carried through with unexampled ease and rapidity. This success, however, would not have been possible, even with the use of the most perfect mechanism, had it not been for the existence of readily available funds in large volume. Although it was promptly announced that the subscriptions to the loan had come from about 4,000,000 persons, the vast majority of whom had subscribed in sums of $10,000 or less, it was not until near the end of July that there was definite knowledge of the fact that more than three-quarters of the subscribers had promptly paid for their bonds without taking advantage of the instalment plan of payment which the government had arranged in order to permit of the easier absorption of the securities. At the same time

it became evident that but a small fraction of the new bonds had been purchased by the banks of the country, while only a very moderate amount had apparently been taken by subscribers who obtained from their banks the funds with which to pay for these bonds. These circumstances, taken together, show that the loan has not only been "popular," in the ordinary sense of that term, but also that it has been possible to reach the ultimate investor and to induce him to take up the securities in a way that largely insures their being held out of the market. A doubly beneficial result has thus been obtained—the quick and satisfactory distribution of these bonds and the assurance that new issues will probably not be disturbed by the presence of floating supplies of this first issue. Not only, therefore, in the amount of the loan, but in the success with which it has been distributed, must this bond issue be regarded as entitled to a very high rank, technically speaking, among the popular loans of the United States.

GROWTH OF WAR EXPENDITURES

As in most wars, it is already turning out that the preliminary estimates of cost are far below what experience shows to be necessary. Upon the entry of the United States into the war it was currently supposed that the total outlay for the first year would probably run to $6,000,000,000 or $7,000,000,000, of which about one-half would be used in the form of advances to the allied nations and one-half for the domestic expenditures of the United States. The first six months of the war, however, have shown that these figures are probably about 40 per cent of the actual requirements. According to the latest estimates, the first year's cost, including both loans to the Allies and domestic expenditures, is likely to run into the neighborhood of $18,000,000,000. Of this sum, apparently, probably something like one-half will be likely to take the form of advances to foreign nations, the remainder being spent in our own military preparations, in industrial undertakings necessitated by the war, and in the payment of ordinary expenses. Congress, which at this writing has not yet passed any measure providing for increased taxation, but is still laboring upon the measure originally proposed to it, thus finds the basis of its calculations altered. The Senate had planned to enact a measure carrying a little more than $1,500,000,000 of taxation, and, in the face of estimates of expenditure that have been multiplied some two and one-half times, it now proposes to raise this figure to a point somewhere between $2,400,000,000 and $2,500,000,000. Estimating that the total outlay for the first year is $18,000,000,000, the proportion

raised by taxation would thus appear to be only about one-seventh of the amount required. This is not quite so small a proportion to be raised by taxation as during the first year of the Civil War, the amount then raised by loans having been as \$8.52 to \$1.00 of taxation. The outcome is displeasing to several groups of persons. At the opening of the war with Germany there had been a section of opinion which favored what was known as "conscription of income," while, on the other hand, some who were socialistically inclined believed that the present was an advantageous time for the application of their favorite theories of proscription of income. Both groups argued strongly in favor of a very large dependence upon taxation relative to loans. Experience, both here and abroad, is showing, however, the necessity of relying in a high degree upon saving as a source of revenue during the present war. No such sums as have been raised in European countries, or as are now to be obtained in the United States, can be deducted from old incomes without either much additional saving on the part of their owners or the creation of new incomes by the saving process. The discouraging effect of taxation upon saving is well known, and the policies thus far pursued by France, England, and Germany show how clearly these countries of scientific taxation have recognized the necessity of relying upon the saving power of the nation, even while applying taxation of an unprecedented character. Apparently the United States is likely to pass through very much the same experience, financially speaking, that has already been had by Great Britain. The legislative discussion of the past few weeks, however, makes it clearer that the controversy between those who believe in the large use of loans and those who desire to limit such loans so far as possible, and to obtain funds through taxation instead, will be continuous so long as the war continues and new revenues have to be provided for.

"TRADING WITH THE ENEMY"

By adopting, in September, the so-called "Trading with the Enemy act" (H.R. 4960) Congress has taken another step toward paralleling the policies of foreign governments as established during the present war. The "Trading with the Enemy act" should be considered in conjunction with the act adopted on June 15, entitled "An act to punish interference with the foreign relations, neutrality, or foreign commerce of the United States," better known as the "Espionage act." In the latter measure there was contained provision for the control of exports and for the requiring of export licenses as a condition of foreign business.

The "Trading with the Enemy act" forbids either direct or indirect commerce with enemies of the United States and also conveys power to forbid imports. Much of the text of the latter act is concerned with detailed provisions relating to the control of banking and foreign exchange operations believed likely to result in benefiting hostile nations, with the technique of patent rights, and the like, during the war period, with the disposal and settlement of contracts entered into prior to the war, and other similar matters. The main purpose of the act is, as already stated, that of preventing either goods or money now in possession of persons resident in the United States, or in other countries trading with the United States, from getting into the hands of citizens of Germany. Many of the provisions of the act are of a restrictive nature, prescribing what conduct or action, ordinarily lawful, will not longer be permitted. From a public standpoint the significant aspect of the measure lies in the fact that it establishes a strict control of foreign trade and prohibits, under severe penalty, either trading itself, or the transporting of goods, for the benefit of "enemies." Under the provisions of this act, taken in connection with the act of June 15, already referred to, a far-reaching transformation in the foreign trade of the United States is being effected. Not only has a system of export licenses been developed, such licenses, for all commodities to which they are applicable, becoming a part of the necessary documentary protection of bank loans, but a general policy of restricting the movement of goods and gold to foreign countries has been inaugurated. The most striking example of the results of this policy is seen in the suspension of exports of food products, copper, and the like to European neutrals, notably Holland and the Scandinavian countries, from which, it is supposed, large transfers have been made to Germany by means of re-exports. The effect of the plan is rapidly proving to be that of limiting the necessary means of livelihood of those neutrals who are now unable to supply themselves either from their ordinary sources elsewhere or from the United States. Not only their trade with Germany, but also their necessary domestic supply of consumable articles, is thus curtailed. One effect of this policy has already been that of considerably sharpening the difficulties of the political position of these European neutrals, who may now be compelled by their necessities, either openly or tacitly, to take sides in the contest. The effect of the export policy upon our own trade abroad cannot thus far be predicted, but from the present outlook it would seem that the principal immediate result would probably be merely that of redistributing goods instead of reducing shipments, practically

everything that can be produced in this country being so strongly in demand as to insure abundant opportunities for its sale.

LEGISLATIVE CONTROL OF FOOD

The foreign economic policy embodied in the two acts already sketched is carried out domestically in the so-called "Food Control act" (Public 41, 65th Congress, first session, approved August 10), whereby there is created a system for the control and use of important products at home. The essential feature of this measure is found in the prohibition of any agreements or conspiracies to limit facilities for transporting, producing, and storing, or dealing in, necessaries of any kind, or the enhancement of the prices of such necessaries. "Hoarding" is forbidden under heavy penalty, and authority is granted for seizing stocks of hoarded articles. The general power of requisition already resident in the hands of the administrative authorities under general law is specifically defined, and conditions of payment for requisitioned articles are prescribed. Quite as extreme as any other element of the act is the provision for the entire or partial suspension of trading on boards of trade and other exchanges; while in line with the general movement toward conservation of food supplies is the prohibition of the use of foodstuffs for distilling from and after a date of thirty days subsequent to the passage of the act. A section which is raising more difference of opinion than perhaps any other is sec. 25, in which authority is granted to the President of the United States to fix prices of coal and coke, and in case of necessity to take over the plants and mines engaged in producing these articles. Work has already begun under the Food Control act for the purpose of conserving and controlling the grain supply, while negotiations with coal and coke producers have been under way for some time past. The question whether the large powers granted in the act will be sufficient to accomplish the same objects that have been attained in other countries remains to be settled. On two points question may be raised: (*a*) whether the control of prices will be effective unless producers are in some way compelled to produce and sell at these prices; and (*b*) whether, even with steady production and sale at fixed prices, consumption can be sufficiently limited by voluntary consent of consumers throughout the country to make the conservation movement really effective and satisfactory in its operation. It is probably true that, at the present time, the further application of the policies embodied in the Food Control act in such a way as to cover production, sale, and consumption would not be sanctioned by public opinion, and the whole policy will necessarily depend for success in practical application upon

the way in which it is administratively developed and upon the attitude adopted toward it by the public in general. This in turn depends upon how far Americans at large feel disposed to go in application of national resources to the support of the European war, since the essential object of the legislation is that of raising our possible exports of foodstuffs to a maximum in order that the fighting force abroad may be currently maintained. The whole food control system, while an outgrowth of necessity, embarks the United States upon a field of enterprise which has heretofore been entirely foreign to its principles and practice of government and which, both in the practical working of the system and in its general effect upon governmental methods and policies, will necessarily have to be developed by a process of experiment.

INVESTMENT EFFECTS OF THE WAR

One important result of war financing is seen in the effect produced upon investment securities of every description. Since the placing of the great government loan of May and June, 1917, there has been a sharp downward movement both in stocks and in bonds, this reduction being distinctively a change in investment values, and not primarily the result of any alteration either in speculative conditions or in industrial outlook. The falling off in the case of some first-class securities has amounted to as much as 10 per cent of their value, the rate of decline varying considerably according to the term the security has to run and the rate of interest it brings. This decline is the result of a complex series of factors. First of all, the placing of the government loan, of course, diverted from their normal channels investment funds which would otherwise have been available and would have been offered for the purchase of existing shares and bonds. Secondly, the establishment of a new and much higher rate of interest on government bonds themselves—the premier security of the world today—undoubtedly changed the underlying basis of income calculation for practically all investments. In addition, the element of tax exemption introduced a factor the importance of which can be only remotely estimated. In the case of some individuals of very large income who were induced by the fact of tax exemption to shift their available funds from private to public bonds the influence may have been very substantial. In the case of other persons of smaller revenue it has been less directly significant, although of some influence. On the whole, it must be reckoned as a factor of considerable, although of eccentric, importance. As a countervailing factor, offsetting these various influences already enumerated, may be mentioned the withdrawal, to a very large extent, of private issues from the market. A very few short-

time refunding or financing operations have been undertaken and carried through, but it is generally admitted that to an increasing extent the fluid wealth of the country must be devoted to the uses of the government and is less and less likely to be readily available for any private or industrial investments. There has thus been brought about, even at this early stage of the war, a striking transformation of the conditions under which capital is borrowed and applied. This and its implied result must undoubtedly be one of the permanently significant influences growing out of the war. Not until the economic pressure on the country is lessened through the reduction of taxation and the withholding of government loans would it again be possible to resume the normal development of other resources and the production of the usual quantity of consumable goods. Meanwhile the supply of such goods would be reduced in proportion to the withdrawal of capital already referred to, and the wants of the population will be progressively more difficult to satisfy as the period subsequent to the suspension of normal investment grows longer and longer. It is a remarkable feature of our war financing that this important result should have been reached so early in the war. In the case of Great Britain it was not fully developed until a much later date. This earlier transformation in the United States is due to the fact that the effects of war financing are immediately and directly felt here, whereas in Great Britain they were in a measure postponed through the placing of a part of the burden, almost from the very outset, upon the British colonies and foreign countries, including the United States. This shifting of the loan to other financial markets necessarily masked for the time being its real consequences and gave opportunity for a continuance of home investment, although naturally this was upon a smaller scale than that which had prevailed before the war. At present there is no possibility of shifting the burden in this war from our own country to other nations. The financial results, therefore, make themselves felt more quickly than they did in Europe.

RESERVE BANKS AND THE WAR

The effect of the war upon the business of the federal reserve banks is now sufficiently advanced to permit of some estimate. Without, of course, being able to anticipate so early and extensive a demand for their services in this connection, the framers of the Federal Reserve act had provided that the banks should act as fiscal agents of the government. Prior to the entry of the United States into the European war these fiscal functions had been but slightly developed. About fifteen months earlier the Secretary of the Treasury had designated the various reserve

banks as public depositaries and had instructed that funds be transferred to them from the local depositary banks in cities in which the reserve banks were located. This resulted in giving the several institutions a moderate volume of deposit and withdrawal business, and the experience thus gained was of great value when the time came for the real acceptance of their fiscal-agency functions. Soon after financial arrangements growing out of our entry into the war had been undertaken the Treasury Department determined to place the whole task of floating the new loans in the hands of local committees, headed in each case by some representative of the federal reserve bank for the district. This has resulted in giving to the reserve banks the leadership in matters of loan organization. At the same time the depositing and withdrawal of funds have been practically turned over to the federal reserve banks, the Gold Settlement Fund at Washington becoming the medium whereby the proceeds of the loan already gathered into the district federal reserve banks are shifted to those parts of the country where they are needed for actual use, either in making advances to the allied governments or in paying for commodities and services on behalf of this government. The result has been to require an immense development of the staffs of the various federal reserve banks, with corresponding increase in expenses. At the same time, however, a much more than proportionate increase in income has been realized by the several banks as a result of rediscounts and purchases made by them in connection with the loan, either for the sake of facilitating the actual lending operations of member banks or for that of relieving the market by returning to it cash which would otherwise have been withdrawn. The effect has been to increase net earnings so rapidly as to enable several of the banks to cover a substantial portion of the dividend payments for which they were in arrears; and, while existing conditions continue, it may reasonably be expected that every reserve bank will, at an early date, have met all of its cumulative dividend requirements and be in position to make a return of surplus income to the government, as provided in the Federal Reserve act itself. The rapid expansion and overshadowing importance of government financial operations has naturally tended to divert the attention of federal reserve banks from operations in which they would otherwise have been interested, but its larger result undoubtedly is that of making the banks, more truly than ever before, effective working organizations, capable of sustaining themselves and of meeting new conditions as they arise. The fact that the final transfer of reserves from the old holders to the new reserve banks has coincided with the beginning of active war work has unfortunately tended to obscure the real consequences of this reserve transfer.

So far as can be judged from the figures, the transfer has shifted to the reserve banks somewhat less than $275,000,000 of reserve money. At the same time the Federal Reserve Board has issued to reserve banks instructions calling for the introduction of a collection system for maturing notes and drafts, thus completing the check-collection system already in force. The banks thus take their places as genuine agencies for the transaction of inter-bank business, as well as for the other business arising between the banks and the government. A broad field of activity and expansion is thus opened to them, and with proper cultivation this increase in service and significance will continue its growth entirely independent of temporary or abnormal war conditions.

THE CAUSES OF UNEMPLOYMENT: A COMMUNICATION

[The editors of the *Journal of Political Economy* have received the following note from Professor H. Stanley Jevons of the University, Allahabad, India, and take pleasure in publishing it in accordance with the suggestion of Professor Jevons.]

Professors of economics and librarians in the United States have experienced some difficulty in tracing a supposed publication of mine entitled *The Causes of Unemployment*, which was mentioned by Mr. D. H. Robertson in his recent book, *The Study of Industrial Fluctuations*. *The Causes of Unemployment* to which this author refers was a reprint of three articles originally published in the *Contemporary Review* of May, July, and August, 1909. When reprinted, it was privately circulated and was not published. It appeared to me, however, that the last of the three articles, which dealt with the causes of the trade cycle, with illustrations from statistics of the United States, was of sufficient permanent importance to warrant republication; and it was published in 1910 by Messrs. P. S. King & Son under the title of *The Sun's Heat and Trade Activity* and with the subsidiary title of "Changes of the Sun's Heat as the Cause of Fluctuations of the Activity of Trade and of Unemployment." It is still obtainable from the publishers; but I have also a certain number of copies available for exchange or presentation, and I have sent thirty copies to the Smithsonian Institution, from which they may be had gratis by university and college libraries, though I should be glad if any university not already exchanging its publications in economics with the *Indian Journal of Economics* would send any such publication in exchange, either to me or to the University Library of Allahabad.